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HOW WILL THE UNITED STATES GOVERNMENT IMPLEMENT THE ENERGY PRIORITIZATION AND ALLOCATION PROVISIONS OF THE DEFENSE PRODUCTION ACT OF 1950

BY

LIEUTENANT COLONEL GREGORY A. RENN

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PRIORITIZATION AND ALLOCATION PROVISIONS OF THE
DEFENSE PRODUCTION ACT OF 1950

AN INDIVIDUAL STUDY PROJECT

by

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U.S. Army War College
Carlisle Barracks, Pennsylvania 17013
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HOW WILL THE UNITED STATES GOVERNMENT IMPLEMENT
THE ENERGY PRIORITIZATION AND ALLOCATION PROVISIONS
OF THE DEFENSE PRODUCTION ACT OF 1950

CHAPTER 1

INTRODUCTION

The United States Military uses approximately .5 million barrels of oil per day to conduct normal peacetime operations. This figure accounts for roughly 2 to 3 percent of the total U.S. requirement for oil. During a major conventional conflict the military demand could be 2 to 3 times this level. According to Department of Energy estimates, this demand would still represent only a relatively small portion of the total U.S. oil consumption.¹ However, other defense related demands for petroleum would also increase, as a result of the need to mobilize the economy, to produce the goods and services necessary to support a war effort. While direct military needs are relatively easy to project, the other "defense support" needs are more difficult to estimate.²

Another factor of significant importance impacting on the ability of mobilization planners to estimate petroleum supply and demand is the fact that every prophecy concerning petroleum made in this country, since 1866, has been wrong.³

In spite of the difficulty in planning and estimating petroleum requirements in scenarios ranging from peace to total war, mechanisms are in place to provide for necessary priorities and allocations in the event that normal supply and/or demand are disrupted. Key among these are the provisions of the Defense Production Act (DPA) of 1950.

The Defense Production Act has been an important legislative tool, since the end of World War II, to counter the continual Soviet threat to the industrial and military fronts.⁴ The DPA has served to create a framework for various levels of defense preparedness ranging from basic peacetime needs, to surge and mobilization capabilities. The basic philosophy of the DPA is to enhance defense preparedness through the maintenance of peacetime programs and policies that can be expanded to provide necessary capabilities during wartime.

The purpose of this study is to examine the evolution of the Defense Production Act of 1950 and to determine how the United States Government would implement the energy prioritization and allocation provisions of the act. Further, some general conclusions will be drawn and some ideas will be provided to improve the identification of the threshold indicators likely to trigger invocation of the prioritization and allocation provisions of this act.

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CHAPTER II

THE BIRTH OF THE DEFENSE PRODUCTION ACT OF 1950

By 1950 the United States had already experienced five years of confrontation with the Soviet Union. It had become clear by this time that the Soviets would be the principal adversary of the United States for years to come. National Security Council Resolution-68(NSC-68), a joint State and Defense Department study, pointed out that the Soviet Union possessed some real and potential military, industrial, and economic advantages over the U.S. The Korean War further highlighted the need for the government to take steps to ensure that increased national security and defense needs could be met while, at the same time, maintaining the nation's economic strength. These facts, coupled with the expansionist goals of the Soviet Union, led to U.S. moves to counter the Soviet threat. An outcome of this effort was the enactment of the Defense Production Act of 1950, designed to counter the Soviet threat on both the military and industrial fronts.¹

President Truman, in his mid-year economic report, outlined the duty of the government to provide for national security and defense. This governmental responsibility is

rooted in economic and political theory as far back as 1776 when Adam Smith first published "Wealth of Nations".²

President Truman expressed his concerns as follows:

The question remains as to how much of our total economic strength must be shifted from peacetime production to defense purposes in the current situation. On the basis of searching study of the best information now available, I have recommended to the Congress the substantially increased programs which should now be undertaken to resist aggression and further build up our preparedness. I have also indicated that other programs will be needed.

The realities of the current situation now require certain changes in national economic policy. These changes will take us in the right direction at once. And if the situation should become even more serious later on, the measures which I now propose for the current situation are also the measures which would make us more ready for further steps.³

President Truman believed there were five changes required to strengthen national economic policy: priority and allocation authority, authority to requisition, provision for the expansion of productive capacity and supply, and control of consumer and real estate credit and commodity speculation.

The Congress acted quickly on the President's proposals. The House Committee on Banking and Currency report, on their version of the Defense Production Act, cited two important facts concerning the situation in which the nation found itself in 1950. First, the national economy was healthy and vital. Second, because the economy was booming, there was little excess industrial capacity that could be easily used to satisfy

increased national defense needs.⁴ The result was a bill that provided a means to channel the necessary materials required by industry to support the national defense.

Although the Defense Production Act of 1950 provided for all the changes to national economic policy requested by the President, only those which deal with the prioritization and allocation functions will be addressed in this study. These provisions, contained in Title I of the Defense Production Act (DPA) specify:

Section 101. The President is hereby authorized (1) to require that performance under contracts or orders (other than contracts of employment) which he deems necessary or appropriate to promote the national defense shall take priority over performance under any other contract or order, and, for the purpose of assuring such priority, to require acceptance and performance of such contracts or orders by any person he finds capable of their performance, and (2) to allocate materials and facilities in such manner, upon such conditions, and to such extent as he shall deem necessary or appropriate to promote the national defense.⁵

THE 1980 AMENDMENT TO THE DEFENSE PRODUCTION ACT OF 1950

Although the Defense Production Act of 1950 has been amended many times, only two amendments specifically address energy issues. The energy crisis of the mid and late 1970s spurred intense activity in the Executive and Legislative branches of government. This resulted from public demands that something be done about this nation's energy problems

instigated by the frustration over long gas lines and higher energy prices. As a result, the Defense Production Act was amended as a part of a comprehensive program to correct the problem.

Although the thrust of legislative action was to encourage synthetic fuels production, this was not the most significant outcome insofar as the Defense Production Act was concerned. The 1980 amendment contained three items that are important to this study. First, the Defense Production Act was extended. Second, it continued to make available, to the President, the broad powers authorized by the original act. Third, and most important, it identified national energy resources as one of the critical strategic materials vital to maintaining the national defense.⁶ This is significant as, prior to 1980, the focus has been concentrated on metals and the principal strategic materials. Now, for the first time, petroleum was recognized as a critical link in defense preparedness.

THE 1986 AMENDMENT TO THE DEFENSE PRODUCTION ACT OF 1950

The most recent amendment to the DPA occurred in 1986. This particular amendment is important because it extends the DPA until September 30, 1989.⁸ If not further extended by Congress, it will expire on this date and leave the nation

without one of its most important mobilization and defense preparedness tools. However, the 1986 amendment continued the Congressional trend begun in 1984 by extending the act for longer periods. Prior to 1984, the DPA was only extended for 1 to 1 1/2 years, as opposed to the 2 1/2 year extensions witnessed in 1984 and 1986.

CONGRESSIONAL INTENT

With each amendment of the DPA, it has been clear that Congress has recognized the need to provide the President the powers necessary to initiate industrial mobilization. However, Congress has been extremely sensitive to the economic dislocation which could occur if the President were to fully invoke the powers authorized by the DPA. Consequently, the Congress has demanded, particularly in the most recent amendments, that the President report and consult with them when certain provisions of the DPA are invoked.⁹ The inference is that Congress demands a role in deciding any action that will have a adverse impact on the economy. While these requirements have very little impact on the Title I provisions, they clearly indicate Congress desires to play a greater role, now and in the future. As a case in point, the Congress has

repeatedly stated strong opposition to any measures which would result in rationing. This was particularly apparent during the debate over the 1980 amendment.

The 1980 amendment also specified three separate requirements for the President to transmit reports and notifications to Congress. The Congress, then has 30 days to either approve or disapprove the Presidents action by resolution. Although not yet directly challenged in court, these provisions have the appearance of a legislative veto and may be unconstitutional. Nevertheless, the key point is Congress is clearly uncomfortable with some provisions of the DPA and may be disposed to either curtail powers authorized the President under the act or under the remotest of possibilities, do away with it altogether- an extreme reaction.

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CHAPTER III

IMPLEMENTATION OF THE DEFENSE PRODUCTION ACT

LEVELS OF DEFENSE DEMAND

In order to more accurately frame the issue of determining implementing triggers to invoke the energy provisions of the DPA, it is necessary to categorize the levels of defense demand which could occur. Although available literature does not agree on the number of mobilization levels, for purposes of this study there are three: peacetime, surge, and mobilization. While it is recognized there are other stages of mobilization, their implications insofar as the Defense Production Act is concerned, would be the same as the three used for this discussion.

The peacetime level assumes that the military and its supporting industrial base are operating on a normal demand basis. That is, the military demand is constant based on current force structure and routine operating frequency. Industrial demand is based on existing contracts for support and on well defined demand for goods and services.

The surge level assumes the military is responding to a particular crisis and the force structure has grown or an increased operating tempo has caused a greater demand.

The mobilization level assumes, both a growth in force structure and an increased operating demand, in response to a crisis requiring mobilization.

Acknowledging these levels of demand, assumptions can now be made concerning the industrial base's ability to meet them. These levels will be used as reference points throughout the rest of this study.

SUPPLY

Supply is more difficult to project than demand as it is based on number of interrelated variables that are difficult to precisely define. As pointed out earlier, all of the energy prophecies made in this country since 1866 have been wrong. Therefore, projecting how and when to implement energy priorities and allocations in the future is an extremely difficult task. Four separate, but inter-related factors impact on determining energy supply requirements: the

reliability of energy figures, time, issue linkages, and the components of the issues.¹ An examination of these factors demonstrate their inconsistencies.

Energy figures are "notoriously manipulable".² The figures can be altered to suit political and economic needs by those who control the resources or generate the figures. For example, the oil industry has, in the recent past, had a great deal of influence in this area since they control the resources. The government also plays a role since the figures can be manipulated to project a more positive or negative outlook depending on the desired political outcome.

Time. Most plans are based on the present environment. However, social, political, and economic conditions are constantly changing. Each change has an impact on the validity of any planning assumption. Therefore, any plan is only as good as the environmental factors that were in existence when the assumptions were formed upon which the plan was based.

The issues affecting energy supply are multi-faceted. Economic, technological, political, ecological, and military issues exist in a complex weave of factors which all impact on energy supply. Any change to one or more of these factors is bound to have an impact on some or all of the others. How large an impact and on how many of the other factors is nearly impossible to predict with certainty.

Issues change based on the situation. All of the issues impacting on energy exist in a given environment and interrelate based upon that environment. If the environment changes, e.g. from peace to war, then the relationship of the issues will change.

Given these facts, it is easy to see how difficult it is to accurately project what the requirements for the supply of energy might be to support a given level of demand. For example, a major conventional war in a non-oil producing region of the world would afford a predictable demand level, but may not necessarily have a severe impact on supply. However, if a major conflict were to occur in one or more oil producing regions there could be a major impact on supply capabilities.

Because the possible combinations and permutations of factors is nearly infinite, it is easy to understand how difficult it is to define a set of triggers to begin the prioritization and allocation process. Nevertheless, the DPA provides a capability to take prioritization and allocation steps when, in the judgement of the President, these actions are necessary.

DPA PRIORITIZATION AND ALLOCATION IMPLEMENTING POLICIES

Executive Order 10480, Administration of Defense Mobilization Programs, delegates the primary responsibility for prioritization and allocation functions (Section 101(a) and (b) respectively) of the Defense Production Act to the Federal Emergency Management Agency (FEMA).³ This responsibility is further delegated to the Department of Commerce which administers the Defense Priorities and Allocations system. Specifics of the Defense Priorities and Allocation System (DPAS) will be discussed in detail later. Under the DPAS the authority to place rated orders (orders placed under the provisions of the DPA which require compliance by suppliers) is further delegated to other agencies, in this case the Department of Defense and Energy.

In order to carry out its responsibilities regarding energy materials, FEMA created Title 44 of the Code of Federal Regulations which states,

(a) Authority of Title I of the Defense Production Act of 1950, as amended, to control the distribution and use of materials and facilities, shall not be used except to require preference in the performance of contracts and orders and to allocate materials and facilities to accomplish the following:

(1) Direct military and atomic energy programs.

(2) Other programs and activities which are related to the military and atomic energy programs and which are certified by the Department of Defense or the Department of Energy and specifically authorized by the Federal Emergency Management Agency.

(3) Deliveries, production, and construction in industry required to fulfill direct military and atomic energy programs and the related programs and activities authorized under paragraph (a) (2) of this section.

(4) The general distribution in the civilian market of materials found to be scarce and critical pursuant to the provisions of section 101 (b) of the Defense Production Act of 1950, as amended, and approved by the director of the Federal Emergency Management Agency under section 201 (b) of Executive Order 10480, as amended.

(b) The distribution of steel, copper, aluminum and nickel alloys for military and atomic energy and authorized related programs and activities shall assure:

(1) That supplies of these materials are available to those programs and activities on time and in proper quantity.

(2) That demands of these programs and activities shall be distributed among suppliers on a generally fair and equitable basis.

(3) That allotments are not made in excess of actual current requirements of these programs and activities.

These criteria shall also apply to the maximum practicable extent to the use of priorities for materials other than steel, aluminum and nickel alloys in support of direct military and atomic energy programs and other authorized programs and activities.⁴

Simply put, as far as energy resources are concerned, the Department of Defense creates the demand, the Departments of Energy and Commerce evaluate supply and will assign priorities and/or recommend allocations. If allocations are required, the issue is coordinated with the Federal Emergency Management Agency.

THE DEFENSE PRIORITIES AND ALLOCATION SYSTEM (DPAS)

Clearly, a mechanism was required to translate policy into action. In 1984 the Defense Priorities System and the Defense Materials Systems were merged to create the Defense Priorities and Allocation System. The DPAS, administered by the Department of Commerce, is the system which implements the prioritization and allocation authorities granted to the President by the Defense Production Act.

The DPAS provides a system for assigning priority ratings for important defense procurement programs. Priority ratings are of two types: "DO" orders and "DX" orders.⁵ Contractors are required to give priority to rated orders, of either category, as necessary to meet required delivery schedules. Most defense related procurements receive DO ratings. DX ratings are reserved for programs having the highest national priority. Under DPAS, the Department of Energy is delegated the authority to place rated orders for programs that maximize domestic energy supplies. The DPAS is designed to be self-administered. However, when production or delivery problems arise, special priorities assistance is available from agencies delegated DPAS authority. An example of an energy problem is evidenced if the Department of Defense projects a shortage of energy supplies that cannot be resolved by internal

reallocation. Special priorities assistance would be requested from the Department of Energy. When the projected shortages are small and will have no impact on the civilian sector, the prioritization function of the DPA is used. However, if the shortage impacts on the civilian sector, then use of the allocation function is required.

The Department of Defense has a well developed system for tracking energy requirements and for initially reallocating supplies when shortages are projected. The Defense Fuel Supply Agency normally has in excess of a 1 to 1 ratio of offered versus required energy supply. In other words, under normal conditions, supply exceeds demand. When the Defense Fuel Supply Agency sees the ratio of offered to required begin to drop, it sends a signal that an energy supply problem could be developing. Additionally, supporting this system the Department of Defense maintains a daily status of fuel stocks available. When these stocks are inadequate, the Joint Materials Acquisition Board can recommend reallocation of supplies among the CINCs. If this step fails to solve the problem, the matter is referred to OSD for resolution or forwarded to the Department of Energy for priorities assistance or allocation. If all of these steps fail to solve the problem the decision could be made by DOE to recommend drawing down the Naval Petroleum reserve and/or the Strategic Petroleum Reserve.

The tracking mechanisms internal to the Department of Defense and DPAS provide a sound means to satisfy defense related needs in the peacetime and surge scenarios. However, the ability of the DPAS to function as effectively in a mobilization scenario may be questionable. This is due to potentially radical alterations of supply and demand which may result from mobilization. The government's policy is that commercial distribution should be governed by the market in all but the most extreme circumstances.⁷ Strengthening this policy is Section 101 (b) of the DPA which only allows prioritization and allocation in the civilian sector if two conditions are met. First, the required material is scarce, critical, and essential to the national defense. Second, that defense requirements cannot be met without causing dislocation and hardship in the civilian marketplace.⁸

There are two possible levels of implementation concerning the allocation function. The scope of the allocation function could be time and/or resource limited. First is, a single resource or group of resources could be subject to allocation controls for a limited or extended period of time. Or, secondly, the government could establish a set of allocation controls which establish a prescribed defense and commercial share of a resource or group of resources.

Government policies and implementing procedures provide an effective framework for meeting defense related energy demands. However, forecasting supply is a complex task which requires more effective procedures to ensure that supply and demand can meet both defense and non defense needs.

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CHAPTER IV

CONCLUSIONS

This study examines the priorities and allocation functions authorized by the Defense Production Act of 1950 and how these authorities are implemented. It is clear that the Defense Production Act provides a means to assure that adequate supplies of materials and services are available to provide for national security and defense needs while, at the same time, preserving the relative vitality of the economy.

The Congress has reaffirmed its support for the Defense Production Act many times over the past thirty-nine years. It has acknowledged the requirement to provide a means to support the needs of national defense by providing the economic tools necessary to meet those needs across the spectrum of possible demands; from peace to surge to mobilization.

The Executive Branch, through its relevant associated departments and agencies, has crafted an extremely effective set of policies and procedures to implement the provisions of the Defense Production Act. These policies and procedures have been streamlined as much as possible and delegate appropriate responsibilities to the proper agencies.

In the case of energy resources required to meet defense needs, the government has a reasonable ability to project demand across the mobilization spectrum, but their ability to project supply is questionable.

The amount of energy required to support normal peacetime military operations, both on the military and civilian sides, has been relatively constant for the past decade. We know the force structure, how much energy is required to keep it operating, and the level of supply necessary for industry to produce the equipment contracted for by the military. We are also able to project, with a high level of assurance, our surge and mobilization military demands, based on existing plans and the size of the force available to be mobilized. Concerning civilian production, energy demands are less easy to determine, but can be fairly accurately projected based on expectations of industrial support necessary to conduct the war effort.

It is the supply side, however, which will have the greatest impact on the implementation of the allocation authority granted by the Defense Production Act. Because the factors impacting on supply are so interrelated and sensitive to change, there is not an effective means to match a given mobilization level with a supply level. An overly optimistic approach in supply projections creates the possibility of inflicting major damage to the economy, and placing the desired

military strategy at risk all because expected supplies are not available. Conversely, a pessimistic supply projection may lead to implementation of an economic and/or military strategy inappropriate to the real situation. Consequently, it appears that, based on the available research, the current approach to the supply situation, favored by the government, is to take it as it comes. The government has effectively said that it will react to situations as they occur and implement actions necessary based on the specifics of the situation. Therefore, the prioritization and allocation functions of the Defense Production Act will be triggered only as needed and based on the situation.

Obviously, military mobilization planners would prefer a more concrete prioritization and allocation plan to support their various levels of mobilization plans. This would allow for a more orderly process and ensure required energy supplies are available to support military and defense related production needs. This is not possible now.

In order to construct a picture of when the functions of the DPA would be triggered, a system needs to be developed to match levels of demand to levels of supply. A computer model could be developed which is capable of measuring all of the supply variables required to produce a linear equation estimating available supply against a given demand scenario. This would be a complex undertaking, considering all of the

variables involved, but would provide a better and more accurate projection of when the allocation function might be triggered compared to the system available now. The ability to predict, with an acceptable degree of accuracy, demand versus supply, would provide a stronger basis for the political, military, and economic decisions required before allocation rules are triggered. Theoretically, with a stronger foundation on which to base their decisions, responsible agencies could react faster, and provide better results.

The Department of Energy is currently working on a Transportation and Refining of Petroleum model which should offer a partial solution to the problem. The Department of Defense should assist and encourage DOE in this effort and continue to refine its own procedures to project demand.

In the mean time, it is safe to assume that energy priorities and allocations authorized by the Defense Production Act will only be triggered when energy supplies become scarce, critical and essential and defense requirements cannot be met without adverse impact on the civilian economy. This implies that the problem must already exist before solutions will be explored. While this is not a prospect to gladden the heart of a mobilization planner, it is probably the only politically acceptable solution until a reasonably accurate method is developed to anticipate supply.

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